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No. 645

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Supreme Court of the United States.

October Term, 1945.

Aldred Investment Trust et al.,

Petitioners,

v.

Securities and Exchange Commission,

Respondent.

PETITION FOR WRIT OF CERTIORARI  
and  
BRIEF IN SUPPORT THEREOF.

HUGH D. McLELLAN,

Attorney for Petitioners.

Of counsel:

WILLIAM J. HESSION.



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# Supreme Court of the United States.

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OCTOBER TERM, 1945.

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ALDRED INVESTMENT TRUST AND GORDON B. HANLON, ROBERT P. LORING, ELTON N. HANLON, W. EDWARD HIGBEE, JOHN L. ARNOLD and MALCOLM M. BOWEN, individually and as trustees and officers of ALDRED INVESTMENT TRUST, AND EZRA D. HART, as trustee of ALDRED INVESTMENT TRUST,  
*Petitioners,*

*v.*

SECURITIES AND EXCHANGE COMMISSION,  
*Respondent.*

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## PETITION FOR WRIT OF CERTIORARI.

*To the Honorable Chief Justice of the United States and Associate Justices of the Supreme Court of the United States:*

Your petitioners, Aldred Investment Trust and Gordon B. Hanlon as president of Aldred Investment Trust, John L. Arnold as treasurer of Aldred Investment Trust, and Robert P. Loring, Elton N. Hanlon, W. Edward Higbee, Malcolm M. Bowen and Ezra D. Hart, all five as trustees of Aldred Investment Trust, and Gordon B. Hanlon, Robert

P. Loring, Elton N. Hanlon, W. Edward Higbee, John L. Arnold and Malcolm M. Bowen, as individuals, respectfully pray that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the First Circuit entered on September 17, 1945, affirming the judgment of the District Court of the United States for the District of Massachusetts entered on January 19, 1945, as amended by order dated January 31, 1945, which permanently enjoined the petitioners Gordon B. Hanlon, Robert P. Loring, Elton N. Hanlon, W. Edward Higbee, John L. Arnold and Malcolm M. Bowen from serving or acting in the capacity of trustee or as an officer of Aldred Investment Trust and which appointed receivers for Aldred Investment Trust under the Investment Company Act.

### **Opinions Below.**

The opinion of the District Court is reported in 58 F. Supp. 724. The opinion of the Circuit Court of Appeals has not been reported. It appears on pages 1101 to 1116 of the Record.

### **Jurisdiction.**

The Circuit Court of Appeals entered its judgment on September 17, 1945, pursuant to an opinion rendered on the same day. Jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925 (28 U.S.C. Sec. 347 (a)).

### **Statute Involved.**

The statute involved is the Investment Company Act of 1940 (54 Stat. 789, 15 U.S.C. Sec. 80(a)).

### Summary and Short Statement of the Matter Involved.

This is an action brought by the Securities and Exchange Commission under the provisions of the Investment Company Act of 1940 seeking to have the individual defendants adjudged guilty of gross misconduct and gross abuse of trust and further seeking the appointment of a receiver for the Trust. Aldred Investment Trust was established by an agreement and declaration of trust dated November 7, 1927. The legal title, complete management and the absolute control of the trust estate vested in the trustees, being five in number (Record, 37). The Trust issued \$10,000,000 face amount 4½% debentures maturing December 1, 1967. Attached to each debenture was one common share for each \$100 principal amount of the debenture. The Trust also issued 112,500 common shares not attached to any debentures. Prior to 1941 the Trust acquired and retired \$4,100,000 face amount of debentures, leaving outstanding 59,000 shares attached to debentures and 112,500 unattached common shares. On or about October, 1941, Gordon B. Hanlon, one of the defendants, acquired by purchase 110,000 unattached shares of the Trust, the total amount of shares then outstanding being 171,500 shares. The individual defendants were officers or trustees of the Trust, all of whom became such after the acquisition of the shares by the said Hanlon.

The case was tried before Sweeney, J. On January 19, 1945, he filed an opinion stating that all of the individual defendants except Ezra D. Hart were guilty of gross abuse of trust and granting the plaintiff's prayer for the appointment of a receiver and saying: "and such receiver will be appointed with the power either to reorganize the capital structure of the Trust or liquidate the Trust and distribute the assets to such creditors, debenture-

holders, and shareholders of the Trust as may be entitled thereto." At no time prior to the opinion or the entry of the judgment hereafter referred to had there been any default entitling any person in interest to a termination or modification of the Trust by liquidation or otherwise. Nor were the holders of the Trust's shareholders' debentures or its other shareholders made parties to or notified of the action.

The judgment of the District Court was also entered January 19, 1945. The judgment, after reciting that the individual defendants except Hart (who remained free to function as trustee) were guilty of gross abuse of trust within the meaning of Section 36 of the Investment Company Act of 1940, and after reciting that the appointment of receivers is necessary to prevent further abuses, enjoined all the individual defendants except Hart from acting in the capacity of trustee or as an officer of the Trust and appointed two receivers with power "to operate the property and business of the defendant Trust in the manner best calculated \* \* \* to protect the business and property and goodwill and value of the rights of the defendant Trust and to prevent the sacrifice thereof." The judgment also required the trustees (including Hart, who was not found guilty of any breach of trust) to turn over all the trust property to the receivers and the Court reserved the right to make such further orders as it might thereafter deem appropriate or proper. An appeal from this judgment was taken February 17, 1945, in behalf of the Trust by all its trustees, its president, its treasurer, and by all the individual defendants except Hart. The Circuit Court of Appeals affirmed the judgment of the District Court.

### Questions Presented.

Two principal questions are now presented for consideration:

— (a) Whether as to each of the individual defendants permanently enjoined from acting as trustee or officer of Aldred Investment Trust the evidence warrants a finding that he has been guilty of gross abuse of trust within the meaning of Section 36 of the Investment Company Act.

(b) Whether as to Aldred Investment Trust the judgment appointing receivers is warranted. This question depends in part on whether the Securities and Exchange Commission has the right under the Investment Company Act to seek the appointment of receivers and whether the Court has the right to grant such relief in a case such as this.

### Reasons for Granting the Writ.

(1) The decision of the Circuit Court of Appeals involves important questions of Federal law which have not been, but should be, settled by this Court. A determination of these issues by this Court appears to be important for the future proper administration of the Investment Company Act.

(2) The decision of the Circuit Court of Appeals to the effect that the trustees (except Hart) and the officers of the Trust were guilty of gross abuse of trust within the meaning of Section 36 of the Investment Company Act is supported by no evidence and is contrary to the evidence.

(3) Because of the far-reaching effects of the decision of the Circuit Court of Appeals as to what constitutes gross abuse of trust under Section 36 of the Investment Com-

pany Act, it is respectfully submitted that this Court should determine whether that decision should be allowed to become the law of the land.

(4) The appointment of receivers for an investment trust on the complaint of the Securities and Exchange Commission where no authority to appoint receivers was granted by the Congress raises an important question which should be resolved by this Court.

(5) The decision of the issues in this case are matters of public importance to the officers and trustees of all investment trusts required to be registered under the Investment Company Act and to the investing public.

(6) The appointment of receivers for an investment trust without the security holders thereof being made a party thereto raises an important question as to all such security holders.

(7) The decision of the Circuit Court of Appeals is seemingly in substantial conflict in principle with the decision of the Second Circuit in the case of *Securities and Exchange Commission v. Long Island Lighting Company*, 148 F. (2d) 252.

(8) The appointment of receivers for an investment trust not in default on any of its obligations as a step in the lower Court's proposed liquidation or reorganization of the Trust calls, we beg to submit, for an exercise of the reviewing powers of this Court.

(9) The appointment of receivers on the sole application of the Securities and Exchange Commission and without making the Trust's debenture shareholders or other shareholders parties to the action and without notice to them deprived them and the Trust of property without due process of law. (*New Orleans Debenture Redemption Company v. Louisiana*, 180 U.S. 320.)

Wherefore your petitioners respectfully pray that this petition for a writ of certiorari be granted.

HUGH D. McLELLAN,  
Attorney for Petitioners.

Of Counsel:

WILLIAM J. HESSON.

**BRIEF IN SUPPORT OF PETITION.****I.****Opinions Below.**

The opinion of the District Court is reported in 58 F. Supp. 724. The opinion of the Circuit Court of Appeals has not been reported. It appears on pages 1101 to 1116 of the Record.

**II.**

**The Court has jurisdiction under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.**

**III.****Statement of the Case.**

The case heard by the Circuit Court of Appeals involved an appeal from a judgment entered on January 19, 1945, by the United States District Court for the District of Massachusetts as amended by an order dated January 31, 1945 (R. 96, 98). The judgment of the District Court permanently enjoined all the individual defendants except Ezra D. Hart from serving as a trustee or as an officer of the Aldred Investment Trust and appointed receivers for the Trust. The main question presented by the appeal from the District Court was whether as to each of the individual defendants the evidence warranted a finding that he was guilty of gross abuse of trust within the meaning of Section 36 of the Investment Company Act of 1940. The main question as to the Aldred Investment Trust was whether the judgment appointing the receivers was warranted. This latter question depended in part only upon the question whether as to each of the individual defendants the injunctions against them were warranted. The questions

here presented grow out of the affirmance of the judgment of the District Court by the Circuit Court of Appeals.

#### IV.

#### Argument.

1. THE CIRCUIT COURT OF APPEALS MISCONCEIVED THE MEANING OF THE WORDS "GROSS ABUSE OF TRUST" APPEARING IN SECTION 36 OF THE INVESTMENT COMPANY ACT AND THE COURT'S CONCLUSION AS TO EACH OF THE INDIVIDUAL DEFENDANTS (EXCEPT HART) THAT HE WAS GUILTY OF GROSS ABUSE OF TRUST AND SHOULD BE ENJOINED WAS WRONG.

Aldred Investment Trust was established by an Agreement and Declaration of Trust dated November 7, 1927, and this instrument is a part of the printed record on appeal (R. 35). The required brevity of a brief in support of a petition for certiorari prevents an attempt adequately to summarize this instrument. All that can here be stated is that the entire trust estate and the absolute control thereof are vested in the trustees, that in case of any vacancy the remaining trustees have power to fill it provided, however, that the shareholders may by majority vote supersede a trustee or trustees and elect new ones. The trustees are to be five in number and to receive compensation at the rate of \$1200 a year (R. 38). The Agreement and Declaration of Trust provides that no investment shall be deemed improper because of its speculative character or because a greater proportion of the trust estate is invested therein than is usual for trustees or by reason of any interest direct or indirect which any trustee may have therein (R. 44). The trustees are authorized to invest the trust estate in securities and obligations of whatever character, "it being the intent that the trustees in their uncontrolled discretion shall have complete freedom in the choice of invest-

ments and reinvestments" (R. 39). The trustees are authorized as owner of any of the trust securities "to exercise all rights of ownership including the right to vote thereon" (R. 39). Provision is made for the issue of shareholders' debentures (R. 55). The holders of the shareholders' debentures are, as we view it, virtually preferred stockholders. At any rate, their claims can be enforced only against the trust property and there is no individual liability on the part of any trustee, officer or shareholder of the trust. The payment of interest on the debentures is in no wise limited to earnings, and the only limitation upon the obligation to pay interest when due is the existence of trust property out of which to pay it.

At its inception the Trust issued \$10,000,000 face amount 4½% debentures maturing December 1, 1967. Attached to each debenture was one common share for each \$100 principal amount of the debenture. The Trust also issued 112,500 common shares not attached to any debentures. Prior to 1941 the Trust acquired and retired \$4,100,000 face amount of debentures, leaving 59,000 shares attached to debentures and 112,500 unattached common shares. In October, 1941, Gordon B. Hanlon acquired by purchase at an auction sale in New York 110,000 unattached shares of the Trust, the total amount of shares then outstanding being 171,500 shares, thus purchasing the controlling shares of the Trust (R. 215, 216). At the time of this purchase the asset value of the Trust was approximately 30% of the face value of the outstanding shareholders' debentures. The cost to Hanlon was approximately \$10,000 paid to the seller and approximately another \$10,000 in revenue stamps (R. 217).

At a shareholders' meeting held on November 18, 1941, the individual defendants Gordon B. Hanlon, Elton N. Hanlon, Robert P. Loring and Malcolm M. Bowen were elected trustees (R. 987), and except for Gordon B. Hanlon

continued to serve as such until enjoined. On January 30, 1943, the defendant Higbee was elected a trustee. On January 17, 1944, Gordon B. Hanlon resigned as trustee and the defendant Hart was elected in his place. On November 20, 1941, Gordon B. Hanlon became president of the Trust, and on November 25, 1941, the defendant Arnold became treasurer of the Trust, and both continued to serve as such until enjoined. Inasmuch as the decision of the Circuit Court of Appeals bases the conclusion that each of the individual defendants except Hart was guilty of gross abuse of trust upon what the individual defendants received or hoped to receive, a statement as to what they received may here be in order.

Each of the trustees received for his services, which involved careful attention to the affairs of the Trust, the \$1200 a year for which the trust instrument provided and nothing more.

Gordon B. Hanlon received for his services as president, which involved the expenditure of a great deal of time taken away from his other business, a salary of \$5500, which was increased to \$6900 in 1943.

The defendant Arnold, whose qualifications appear in an appendix hereafter referred to, devoted all his time to the treasurership of the Trust, for which he received a salary of \$3500 at first and which, when the asset value of the Trust had greatly increased, was raised to \$4500 a year.

As secretary of the Trust the defendant Loring received a salary of \$300 a year and he devoted a great deal of time to the books and records of the Trust.

For completeness's sake it should be here added that the trustees voted to terminate the office facilities of the Trust located in New York and to establish its business offices in the suite of Gordon B. Hanlon & Co. at 100 Milk Street, Boston, and to pay \$410 per month for various facilities and services as follows: rent, light, telephone (local), ste-

nographer, bookkeeper, statistician, statistical, etc., services, miscellaneous facilities (typewriters, etc.), furniture and fixtures (R. 994, 995, 999). There is no finding by either Court that the charge for these facilities was excessive, and the evidence shows that it is less than was paid for like services under the former management. Nor is there any finding by any judge that the salaries above referred to were unreasonable, excessive or not fully earned.

The decision of the Circuit Court of Appeals, as well as that of the District Court, refers to the appearance of Gordon B. Hanlon before the Securities and Exchange Commission in connection with a proposed tentative plan or plans of recapitalization. In January, 1942, when the affairs of the Trust were at a low ebb, the defendant Hanlon desired to bring about a plan of recapitalization which would obviate the necessity of selling securities at depressed prices in order to meet the necessary interest payments. He had a right without resort to the Securities and Exchange Commission to submit such a plan to the security holders, and the Commission had the right to seek a Court injunction against carrying out the plan and to obtain it if the Court should find the plan grossly unfair (15 U.S.C. Sec. 80a-25(c)).

At the time when the employees of the Securities and Exchange Commission were considering the tentative plan and its various modifications, it was their fixed determination, not then made apparent to Hanlon, to prevent any plan going into effect which did not deprive Hanlon of the voting power of the stock which he had bought and paid for. These negotiations began in January, 1942, and while apparently still under consideration Hanlon inquired of the Securities and Exchange Commission as to whether there were any points in the plan of recapitalization which appeared to need additional consideration (R. 970). No acknowledgment of this letter was ever sent, and instead

Hanlon was advised that if he endeavored to carry the plan into effect the Commission would feel it necessary to institute proceedings to enjoin him (R. 971). Thereafter no attempt was made to put the plan into effect. This being the attitude of the Commission, Hanlon, who had already suggested the sterilization, so far as voting power was concerned, of 85,000 shares of his stock (R. 680), took no action looking to the presentation by the trustees of a plan of recapitalization to the security holders. In the course of the proceedings before the Commission Hanlon recommended against liquidation and gave his reasons (R. 909, 910). The reason the Trust was not liquidated was because neither Hanlon nor the other trustees believed that such a course would be in the interest of the Trust, and they were right about it. The asset value of the Trust in January, 1942, was approximately \$362 per \$1000 debenture. The asset value as of December 30, 1944, was somewhat in excess of \$670 per \$1000 debenture (R. 829).

The opinion of the Circuit Court of Appeals, after pointing out that Hanlon could not gain by liquidating, goes on to say: "The awareness of this conflict of interest is further suggested by the action of the Trustees in December 1942 when they voted to pay salaries in advance instead of paying them a week after they were due." We do not see exactly how the avoidance of a possible preference under the bankruptcy law shows the awareness of a conflict of interest or constitutes any evidence of gross abuse of trust, and especially where bankruptcy would have caused an irreparable loss to the security holders.

The opinion of the Circuit Court of Appeals next states: "Moreover throughout 1942 and 1943 the Trust engaged in selling securities to meet its running expenses and interest charges.<sup>a</sup> The Court considered this to be a return of capi-

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<sup>a</sup> This became unnecessary in 1944 (R. 829, 901).

tal in the guise of interest. It pointed out that no technical act of default could occur so long as the appellants could sell securities and pay out the proceeds as 'ostensible interest', that this left the debenture holders helpless 'under the terms of the debenture instrument to halt the dissipation of assets' and concluded that so long as the 'personal advantage' of the appellants stood in the way, the debenture holders could not expect relief either by way of bona fide recapitalization or liquidation." It is perfectly true that the Trust sold securities to meet running expenses and interest charges. This the Trust was bound to do under the terms of the shareholders' indenture, and we are unable to see how the defendants can be regarded as guilty of an abuse of trust for doing that which they were bound to do. Moreover, Mr. Hanlon had done his best before the Securities and Exchange Commission to get the approval of a plan for recapitalization which would have been in the interest of the debenture shareholders and would have obviated the necessity of the sale in a depressed market of securities for the purpose of paying interest.

The opinion of the Circuit Court of Appeals recites in substance that the Trust purchased the controlling shares of Eastern Racing Association and paid a premium for control. Neither the District Court nor the Circuit Court found that this investment was improper. There was no evidence that any premium for control was paid by the Trustees. It is true that the price paid was greater than the price recently bid over the counter for odd lots of this stock, but the price of \$80 a share was in the light of the history of the Association, its earnings and its assets, so low that the District Court would not hear counsel for the defendants upon the subject (R. 1050). Indeed, the facts established by the evidence are that after following for years a policy of liberal depreciation the book value of Eastern Racing stock was well in excess of \$80 a share and

its earnings had been steady and large. If it had to go out of business, the liquidation value of each share of stock upon the testimony, not only of the defendants' witness (R. 404-417) but also of the plaintiff's so-called expert (R. 811, 812, 813), would have exceeded the purchase price, and this upon the assumption that all its real estate and buildings were sold for \$1. It is not the position of the petitioners that the stock was bought with an intention to liquidate, but consideration of the value of the stock for which it would liquidate in the event of an unexpected loss of the right to do business was an important element in the determination of the safety of the investment. The opinion of the Circuit Court of Appeals says in substance that the Trust, in order to obtain sufficient money to pay for the Eastern Racing Association shares, sold stocks which Hanlon had in 1942 advised against selling. In 1942 the stock of Pennsylvania Water & Power Company was selling in the low 30's and Consolidated Gas, Light & Power Company of Baltimore was selling in the 30's, while when they were sold in the latter part of 1943 or early 1944 the Trust received a price for each of them in the 60's. Hanlon was right in advising against the selling of these securities at 30 when, as it turned out, they were later sold in the 60's, and notwithstanding anything in the opinion of the Circuit Court of Appeals the evidence establishes conclusively the fact that these stocks were sold at the best obtainable price.

The opinion of the Circuit Court of Appeals refers to an application made by Hanlon to the Wage Stabilization Board for the approval of two new executive positions to be held by the former president and former treasurer of the Association and to Hanlon's objection to the action of the Board upon that application. The paragraph of the opinion ends with the statement that "It is apparent from the face of the record that Hanlon's testimony with respect

to salaries was equivocal and evasive." The testimony to which the Court refers appears on pages 290 to 294 of the record and there is nothing equivocal or evasive about it. See in this connection also the testimony of Walter F. Burke, head of the Regional Office, Salary Stabilization Unit, Treasury Department, who was called as a witness by the plaintiff (R. 755).

This Record contains no evidence, direct or indirect, that any of the individual defendants ever received a penny for the services rendered by them to Eastern Racing Association, nor is there any evidence, direct or indirect, that any of them ever expected in the future to receive any compensation from Eastern Racing Association except such as might be a fair return for services rendered. There was plenty of opportunity for the Directors to vote themselves salaries and receive compensation, but this was never done. Had it been done, the Directors would have been guilty of no abuse of trust in their relations either to Eastern Racing Association or to Aldred Investment Trust. We submit that the law upon this subject is that a trustee may receive compensation as an officer of the corporation, shares of which he holds in trust, even though the shares represent a controlling interest in the corporation, if he performs necessary services as such officer and receives no more than proper compensation for such services. See Restatement of the Law of Trusts, sec. 170(n), p. 439. Nor, we submit, is it improper for a trustee or officer of a trust to participate in the acquisition for the trust of a controlling interest in a corporation because of the fact, if it be a fact, that he contemplates becoming an officer of the corporation, performing necessary services for it and receiving reasonable compensation for such services, and this is so even though the trust instrument should say nothing upon the subject. We requested the District Judge so to rule and argued the question in our brief submitted to the

Circuit Court of Appeals, whose opinion contains no direct reference to the request but seems to proceed upon the assumption that it is not the law. Moreover, by the terms of the shareholders' debentures themselves, which refer to the Agreement and Declaration of Trust, the rights of the debenture holders are limited by the provisions of the Declaration of Trust, which provides:

"No investment or reinvestment shall be deemed improper because of its speculative character or because a greater proportion of the Trust Estate is invested therein than is usual for trustees, or by reason of any interest, direct or indirect, which any Trustee or any Shareholder or any officer of the Trust, or any of them, either individually or in any representative or fiduciary capacity, may have therein, or by reason of any profit that they or any of them may make therefrom," etc. (R. 44, 45).

By virtue of this provision of the trust instrument the defendants had a perfect right to purchase control of Eastern Racing Association even though that purchase might, as it did not, result in a benefit or profit to themselves.

Aldred Investment Trust has been registered with the Securities and Exchange Commission pursuant to the Investment Company Act of 1940 (15 U.S.C. Secs. 80a-8) since October, 1941, as a closed-end, non-diversified management investment company. The Trust's Registration Statement contained the requisite recital of the Trust's policy with reference to concentrating investments in a particular industry or group of industries. Space does not permit an adequate statement of that policy, which may be found beginning with page 879 of the Record. We do not pretend to know whether under the terms of the investment policy there stated a purchase of control of Eastern Racing Association was permissible. Section 13A of the Invest-

ment Company Act provides that no registered investment company shall, unless authorized by the vote of a majority of its outstanding voting security holders, deviate from its policy in respect to concentration of investments in any particular industry or group of industries as recited in its registration statement. Accordingly, it was decided to hold a shareholders' meeting for the purpose, among others, of considering and voting upon future investment policy of the Trust. It was not for the shareholders to determine what investments should be made. It was not for them to decide whether the shares of Eastern Racing Association should be acquired. This, under the Agreement and Declaration of Trust, was a matter solely for the trustees, and the Investment Company Act contains nothing depriving the trustees of this power.

Under date of December 16, 1943, a notice of annual meeting of shareholders was prepared, a copy of which notice appears at page 591 of the Record. It gives notice of a meeting of the shareholders to be held January 24, 1944, for the purpose of taking action upon the following matters:

"To see if the shareholders will ratify or reject the selection by the Trustees of Touche Niven & Co. as independent public accountants to audit the accounts of the Trust for the calendar year 1944.

"To consider and vote upon future investment policy for the Trust.

"To see if the shareholders will vote to supersede or re-elect the Trustees now in office or any of them or elect a new Trustee or Trustees to fill any vacancy which may exist at the time of the meeting."

The notice is signed by Aldred Investment Trust by R. P. Loring, Secretary. After it had been prepared it was

submitted to the law firm of Putnam, Bell, Dutch & Santry, who had been acting as counsel for the Trust since the fall of 1941 (R. 374), who passed on its legality and who later advised that the purchase of the Eastern Racing Association was perfectly legal and proper (R. 375). The reason for the foregoing statement as to the annual shareholders' meeting and the notice thereof is the most extraordinary manner in which the District Judge and the Circuit Court dealt with this matter. The District Judge found the notice a "masterful bit of understatement" and the Circuit Judge quoted this statement with apparent approval. The opinion of the Circuit Court of Appeals dealing with this aspect of the case shows, we respectfully submit, a misunderstanding of the functions of the trustees and the shareholders under the Agreement and Declaration of Trust. Nor do the Honorable Judges seem to have given consideration to the situation which existed on December 16, 1943, when the notices were sent. At this time there had been only preliminary negotiations for the possible purchase of the Eastern Racing Association stock. No commitment had been made by either side, and so far as appeared no price had been arrived at. A promise had been made to the owners of the stock not to make public the negotiations. If there had been no such promise, it is inconceivable that a prospective purchaser would send out notices broadcasting the fact that the owners of the Eastern Racing Association stock had finally arrived at a point where they were ready to consider selling.

We do not propose to violate the rule as to brevity in this sort of proceeding or waste the time of this Court by here attempting a discussion of what the Court of Appeals has to say about a broker's letter of January 15, 1944, to Aldred Investment Trust or Mr. Arnold's reply thereto. The letters appear on pages 110 and 111 of the Record and justify no such criticism as the District Judge and the

Circuit Judge make of them. Is it conceivable that a prospective purchaser who had no commitment from a prospective seller would write an investment broker that negotiations were in progress and that the seller had at least arrived at a point where he would consider making a sale of his stock? Moreover, we find in the Record no evidence that the trustees as opposed to one of the officers of the Trust ever saw this correspondence. The Trust received an option on the Eastern Racing Association stock on January 24, 1944, and the option was later taken up and the transaction was completed the latter part of February, 1944. The Trust received, under date of March 22, 1944, a letter, not from a debenture holder but from a dealer in investment securities, and the Trust treasurer replied thereto under date of March 25, 1944. These letters appear at pages 1046 and 1047 of the Record. They show that Mr. Arnold, as treasurer of the Trust, entertained the view that furnishing interim information to one security holder but not to all would tend to be inequitable and relatively unfair to the shareholders themselves. In view of the fact that the inquiry came, not from a debenture holder, but from a dealer in investment securities, Mr. Arnold might well have been subject to criticism if he had entertained a different view. It was these very letters to which the Circuit Court of Appeals referred in that portion of its opinion reading: "Even in March after the transaction had been completed the Trustees were following a policy of evasion and equivocation with the debenture holders." As to this statement, perhaps it should here be added that there was no evidence that the trustees knew of this correspondence, and if they had known of it, the correspondence would not have warranted the statement that the trustees were following any course of evasion and equivocation with the debenture holders. The inquiry was not that of a debenture holder, did not purport to be made upon the authority of a debent-

ture holder, but was merely that of a dealer in investment securities.

There is, we submit, in this whole Record no evidence warranting the conclusion that Gordon B. Hanlon, the Trust's president, Robert P. Loring, a trustee and secretary of the Trust, or John L. Arnold, the treasurer of the Trust but not a trustee, failed in any respect to act in the interest of the Trust or was guilty of any abuse of trust. As to them the decision of the Circuit Court of Appeals that they were guilty of gross abuse of trust is clearly wrong. But the so-called relief sought by the plaintiff manifestly could not have been granted unless the other defendants were swept into the case by the following statement appearing in the opinion of the Circuit Court of Appeals, namely: "We are not disposed to question the conclusion of the District Court that 'at all times the Trustees have been subject to Hanlon's wishes and directions'." The Record contains no evidence warranting any such statement.

Thinking that the Court might like to know something of the training and experience of these petitioners as disclosed by the Record, we annex hereto an appendix designed to furnish this information.

2. THE CIRCUIT COURT OF APPEALS ERRED IN AFFIRMING THE JUDGMENT OF THE DISTRICT COURT APPOINTING RECEIVERS EVEN IF IT BE ASSUMED, CONTRARY TO THE FACT, THAT SOME OR ALL OF THE DEFENDANT'S TRUSTEES EXCEPT MR. HART WERE PROPERLY ENJOINED FROM ACTING AS SUCH.

At the outset attention may be called to the fact that Mr. Hart was not enjoined, that Mr. Hanlon still owned a majority of all the voting securities of Aldred Investment Trust, that neither the Court nor the Commission had any power to control his power to elect new trustees, and that accordingly there was no such necessity for the appoint-

ment of receivers as to render such an appointment valid. But there are other reasons why the Court was without power to appoint receivers over Aldred Investment Trust. The Investment Company Act contains no authority for the liquidation of a trust or the appointment of a receiver or trustee for any violation of Section 36 of the Act. That the Congress was aware of its powers in a proper case to provide for liquidation of a trust and the appointment of a trustee is shown in other parts of the Act.

Section 42(e) provides that, if any person is engaged or is about to engage in any act or practice in violation of this title, the Commission may bring an action in the proper court of the United States to enjoin such acts or practices and to enforce compliance with this title.<sup>a</sup>

There is nothing in the first sentence of this section providing for the appointment of a receiver or for an order of liquidation. However, it is significant that this section further provides that, in any proceeding to enforce compliance with Section 7 of the Act, the Court, as a court of equity, may take exclusive jurisdiction of an investment company and shall have jurisdiction to appoint a trustee, who, with the approval of the Court, shall have power to dispose of any or all of the assets subject to such terms and conditions as the Court may prescribe.

It is not alleged in the complaint nor was it contended at the trial that the Aldred Investment Trust has violated the provisions of Section 7, which relates only to unregistered companies. On the contrary, paragraph 1 of the complaint specifically states and the evidence shows that the Aldred Investment Trust was an investment company registered with the Securities and Exchange Commission pursuant to the Investment Company Act of 1940. Thus it is quite obvious that the Congress was not unmindful

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<sup>a</sup> The title referred to reads: "Title I—Investment Companies."

of its powers to authorize courts to order a liquidation of a trust because in this subsection (Section 42(e)) it is specifically provided for such liquidation in a proper case. That the Congress specifically limited the powers of the Court under the provisions of the Act to order a liquidation of a trust is further emphasized by the provisions of Section 26(c), wherein it is provided that, whenever the Commission has reason to believe that a unit investment trust (which Aldred is not, see Section 4(2)) is inactive and that its liquidation is in the interest of its security holders, the Commission may file a complaint seeking the liquidation of such trust in the District Court of the United States in any district wherein any trustee of such trust resides. The section further provides that, if the Court determines that such liquidation is in the interest of the security holders of such trust, the Court shall order such liquidation and the distribution of the proceeds to the security holders in such manner as may appear equitable to the Court.

It is only in these two classes of cases that the Investment Company Act authorizes the Commission to bring an action for the liquidation of a trust, and it is apparent that the alleged misconduct of the trustees comes under neither provision.

Section 44, under which the complaint alleges that this action arises, provides that the District Courts of the United States shall have jurisdiction of violations of this title and of all suits in equity or actions at law brought to enforce any liability or duty created by, or to enjoin any violation of, this title. There is nothing in Section 44 that authorizes either the appointment of a receiver or an order of liquidation of this Trust. Clearly enough the Commission is not empowered under the provisions of the Investment Company Act to bring an action for the appointment of a receiver of an investment trust on the facts

alleged in the complaint and that the District Court had no authority under the provisions of the Act either to appoint a receiver or to enter an order of liquidation and distribution of the assets of the Trust.

The District Judge in his memorandum of decision upon the defendants' motion for dismissal of the complaint denied the motion, saying:

"It is true that Section 42e of the Investment Act of 1940 specifically authorizes the court to appoint a receiver for violations of Section 7 of that Act, but this is not a limitation upon the powers of a court of equity to appoint a receiver but is, rather, in addition to such powers as are inherent in such a court. Such was the decision of the court in *S.E.C. v. Fiscal Fund*, 48 Fed. Supp. 712" (R. 99).

In that case there was no opposition to the appointment of a receiver. The hearing was entirely *ex parte*. In that case the defendant had no management. Four of the five directors had resigned and the president of the company, who was its only director and only officer, was out of the country with the Armed Forces, and therefore unavailable. In the case at bar Mr. Hart, who was not found guilty of any abuse of trust and was not enjoined, is still on the board of trustees, and Mr. Hanlon, as the owner of the voting control of the Trust, has the power, with which no one has any right to interfere, promptly to supersede the enjoined trustees and elect new trustees. Under the circumstances above stated, the Fiscal Fund case can hardly be regarded as sufficient authority for the appointment of receivers in the case at bar. Analogous to the situation here presented are the facts and decision in *Securities & Exchange Commission v. Long Island Lighting Company*, decided February 23, 1945, by the Circuit Court

of Appeals for the Second Circuit, 148 Fed. (2d) 252. In that case, the plaintiff sought temporary and permanent injunctions restraining the defendant from consummating a plan for its recapitalization until determination of proceedings pending before the Commission involving the status of the defendant under the Public Utility Holding Act of 1935. The District Court had denied the preliminary injunction on the ground that it lacked power to grant the relief sought. The Circuit Court of Appeals affirmed the decision of the District Court, called attention to the fact that there was no specific grant in the statute of a right to an injunction, and denied that under its general equity powers it had the power to grant the relief sought. In reaching these conclusions, two of the judges of the Circuit Court of Appeals used language particularly germane to the question whether under its general equity powers the District Court in the case at bar had the power to appoint receivers for Aldred Investment Trust.

Judge Simons states:

“The Commission asserts, however, that it does not rely for its authority to seek relief, upon any specific grant of the statute. It disclaims reliance upon §18 (f) as a basis for the jurisdiction of the court, for that section grants its authority to bring an action in a proper district court of the United States only for acts or practices which constitute or will constitute a violation of the provisions of the Act, or of any rule, regulation, or order thereunder, and it concedes there have been no such violations. It plants itself squarely upon the general equity powers of District Court under §24 of the Judicial Code which extend, *inter alia*, to all suits of a civil nature at common law or in equity, brought by the United States or by any officer thereof authorized by law to suit. In support of its position

it argues that the various branches of the federal government have certain implied and inherent powers which will be exercised, where appropriate, to protect the proper functioning of another branch of the government, that preservation of the *status quo* pending determination, is a traditional aspect of equity jurisdiction, and that the circumstances of the present case amply warrant its exercise to prevent circumvention of the Commission's jurisdiction under the Holding Company Act. It deems it an unnecessary refinement to determine whether particular cases relied on rest upon the fact that the action is brought by the United States or by an officer thereof authorized to sue, or upon the existence of a federal question, or upon the ground that the case falls within §24 (8) of the Judicial Code applicable to 'all suits and proceedings arising under any law regulating commerce'. In seeking injunctive relief the Commission asserts it is asking the court to exercise the same kind of jurisdiction which a federal court would employ to protect its own jurisdiction, and to preserve a *status quo* pending proceedings before another tribunal.

"While the Commission does not base its suit for relief upon any express authority conferred upon it by the Act, but rests its case upon the general equity powers of a federal court, it is not without importance that, by the terms of the Act which purport to provide for a comprehensive scheme for control of practices by public utility holding companies and affiliates affected with a national public interest, the Congress conferred upon the Commission in §18(a) and §11(d), the power to invoke the aid of the courts only to prevent evasions of the Act and non-compliance with the orders of the Commission. There is concededly no power to restrain or discipline holding companies exempt from its pro-

visions. It would seem, therefore, that the guide to statutory construction in the maxim *expressio unius exclusio alterius*, is applicable. Express powers are generally construed to be in negation of powers not expressly granted, and the application of the maxim here is not such an unwarranted use thereof as it was found to be in the *Continental Ill. N.B. & T. Co. v. Chi. R.I. Co.*, *supra*, where it required other provisions of law to be ignored."

As above indicated, there was a concurring opinion in *Securities & Exchange Commission v. Long Island Lighting Company*, *supra*, which was written by Judge Hutcheson, who said:

"I concur in all that is said in Judge Simons' excellent opinion. I think, though, that the short and simple answer to appellant's claim of jurisdiction is to be found in the fact that Section 25 . . . of the Public Utility Holding Company Act, which defines the jurisdiction of the federal courts with respect to suits brought by the commission does not grant jurisdiction of a suit of this kind. I write this brief concurrence to say so. I think it may not be doubted that this section and Sections 11 (d) (e) (f) and 18 (d) (f), which state the circumstances and the manner in which the commission can apply to the courts for relief, were intended to be, and are, as to jurisdiction, both inclusive and exclusive. A word by word examination of these sections makes it clear that nothing in them authorizes the suit here brought. Indeed, the commission in its brief disclaims them as the jurisdictional basis of the suit. In my view, this disclaimer, in the light of the settled rule of law that a statutory scheme intended to be all inclusive must be treated as exclusive also, settles

the controversy against the commission. For it is of the essence of such a scheme that what is not included is excluded. The commission, therefore, in asserting a roving commission to sue for, or as, the United States, *In Re: Debs*, 158 U.S. 564, finds itself confronted with the difficulty, inherent in efforts to induce a court of special jurisdiction to embark upon the exercise of jurisdiction, vague in its generality, and general in its vagueness. But this is not all. It finds itself confronted with the one of attempting to sue out of the character with which the law has invested it, of invoking a jurisdiction beyond that to which the statute, by especially defining, has limited it. It seems quite clear to me that unless we are not to abandon in favor of notions completely alien to our system of law, the settled doctrines of federal jurisdiction and of statutory construction prevailing here, we must say: that the commission is the creature of statute; that it lives and moves and has its being by statutory authority alone, and only within statutory confines; that the creature may not say to its creator, 'Why hast thou created me thus?'; and that the commission may not, therefore, by any kind of mysterious metempsychosis, become disembodied from, and disenthralled of, the statute which gives it life, to sue not as creature but as creator, in short, as the United States itself. Because then the statute of its creation does not grant but in effect denies, the jurisdiction invoked, I am in no doubt that the district judge was right and that his judgment should be affirmed."

We submit that the power of appointment of a receiver is a delicate one and is not to be lightly inferred. This is especially true where the Act confers the power to appoint a trustee under some circumstances and fails to confer it under other circumstances. Receivership is a harsh and

drastic remedy and is to be resorted to only under extraordinary circumstances. See also *Hermamos v. Puerto Rico*, 118 Fed. (2d) 752, 758, where Judge Magruder, quoting from another case, says:

“It is perhaps unnecessary to advert to certain well-settled principles governing the appointment of receivers. It is a drastic remedy, and calls for the exercise of the greatest care and judgment; and this is especially true where it is sought to take not only from the parties themselves the management of their own property but property in the hands of a trustee.”

In concluding this branch of the brief we respectfully urge that the District Court's appointment of a receiver was clearly erroneous for the following reasons, among others:

- (1) The Investment Company Act confers no such power upon the Court.
- (2) No such power exists under the general equity powers of the Court.
- (3) The defendants were guilty of no gross abuse of trust and should not be deprived of the possession and control of the trust estate which the trust instrument gives them.
- (4) Even if, as is contrary to the fact, any defendant was guilty of breach of trust, some of them were not and they should not be deprived of the control of the affairs of the Trust which the trust instrument gives them.
- (5) The defendant Hart, one of the trustees of the Trust, has been found guilty of no abuse of trust and is still a trustee.
- (6) Gordon B. Hanlon owns a majority of the voting securities of the Trust, and the Court has no power to deprive him of that control and no power to

deprive him of the right to supersede the enjoined trustees with other trustees.

3. THE PORTIONS OF THE RECORD HERETOFORE DISCUSSED AND THE WHOLE RECORD SHOW, WE RESPECTFULLY SUGGEST, THAT THE WRIT SHOULD BE GRANTED FOR EACH OF THE REASONS STATED IN THE PETITION FOR CERTIORARI, WHICH REASONS NEED NOT HERE BE REPEATED BUT ARE EMBODIED HEREIN BY REFERENCE.

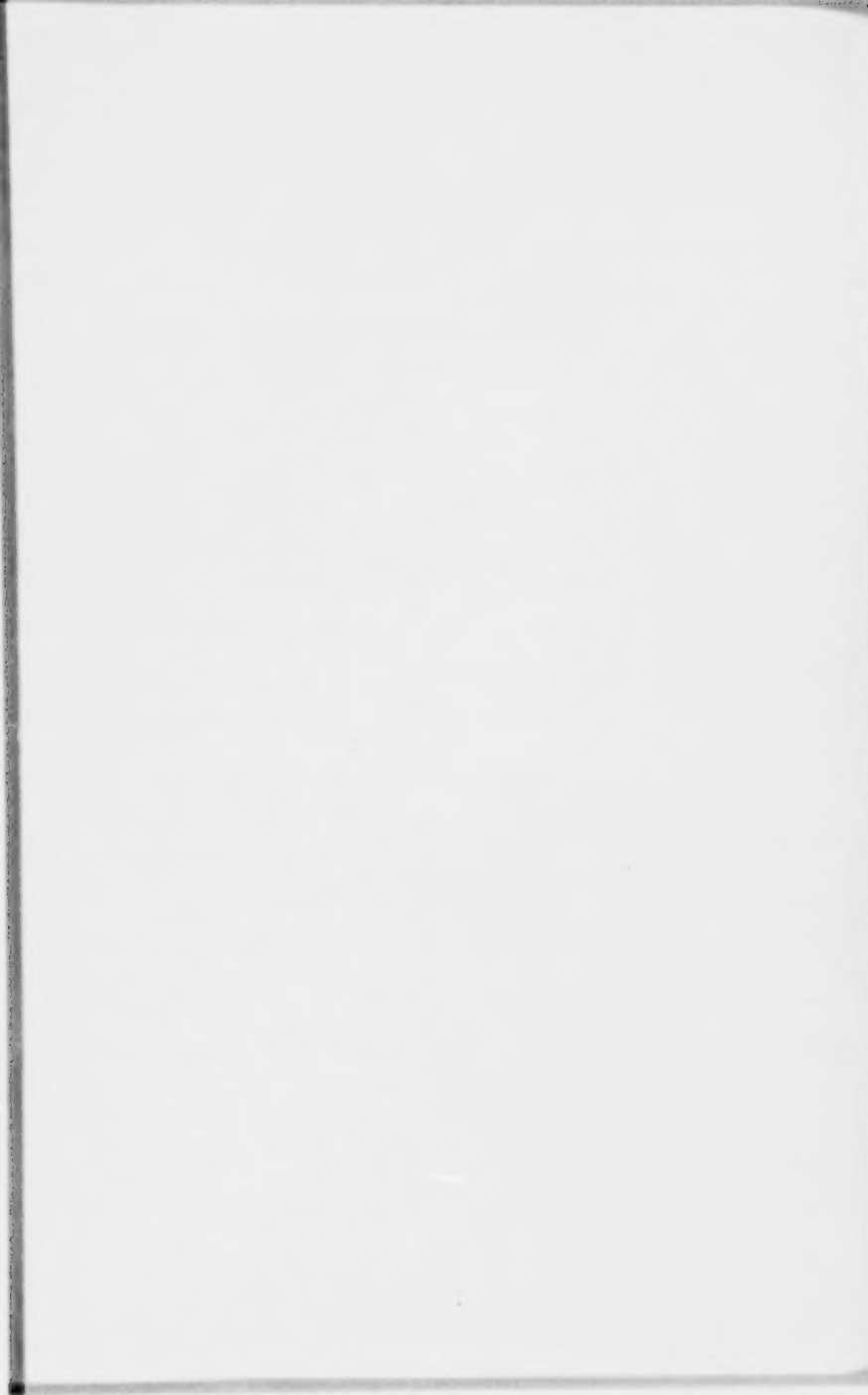
Respectfully submitted,

HUGH D. McLELLAN,  
Attorney for Petitioners.

Of Counsel:

WILLIAM J. HESSION.





**Appendix.**

Gordon B. Hanlon was elected a trustee of Aldred Investment Trust by a vote of the shareholders on November 18, 1941, and served as such until January 17, 1944, at which time he resigned as a trustee. He was elected president of Aldred Investment Trust on November 20, 1941, at a special meeting of the trustees, and continued to serve in such capacity until enjoined. He is a stock broker, bond broker and bond dealer, doing business under the name of Gordon B. Hanlon & Company. He is thirty-seven years of age. He graduated from Dorchester High School in 1925 and shortly thereafter became registered as a salesman at a bond house in Boston and was in the sales department of that firm for two years. He then purchased an interest in and became vice-president of a brokerage concern. There he remained as vice-president until 1932, when he opened an office under the name of "Gordon B. Hanlon & Company" and he has conducted his brokerage and bond business under that name ever since. Between 1925 and the date of the trial of this action he took various courses for the purpose of preparing himself for the conduct of his business and for the purpose of qualifying himself in the analysis of stocks, bonds and general business conditions. To that end he attended law school for three years and took special courses at the Harvard Business School in 1930 and 1931, where he was also enrolled in the years 1934, 1935 and 1936. He studied taxation at Bentley Accounting School and completed courses in taxes. At the Harvard Business School he took an extensive course in public utilities, economic management and finances, and a full year's course in interpretation of financial statements and auditing. He took also a full year's course in investment management and investment counsel work and a full year's course with Professor Sprague in monetary problems, policies and taxation. He

owns a seat on the Boston Stock Exchange and does a commission business there in addition to having a large amount of dealer business (R. 213, 214, 334, 335).

Robert P. Loring was elected a trustee of Aldred Investment Trust at a meeting of the shareholders held November 18, 1941. He was elected secretary of the Aldred Investment Trust at a meeting of the trustees held November 25, 1941. He continued to act in both of these capacities until enjoined. He is a graduate of the Swampscott High School and in 1935 graduated from Bentley's School of Accounting and Finance. He then entered the employ of Gordon B. Hanlon Company, where his work consisted of accounting, statistical work and the handling of and trading in securities (R. 122, 123, 342, 343, 564).

Elton N. Hanlon was elected a trustee of Aldred Investment Trust by the shareholders at a meeting held November 18, 1941, and continued to serve in that capacity until enjoined. A brother of Gordon B. Hanlon, he had been in the brokerage business and had a large amount of experience with the firm of Southgate and with Thorton, Curtis & Company (R. 341, 425).

W. Edward Higbee was elected a trustee of Aldred Investment Trust at an annual meeting of the shareholders on January 30, 1943, and continued to serve in that capacity until enjoined. At Massachusetts Institute of Technology he was a member of Phi Beta Kappa, graduated from Technology in 1929 with a degree of Bachelor of Science, and received the degree of Doctor of Philosophy from the same institution in 1933. In October, 1934, he became a member of the staff of Massachusetts Institute of Technology, where he remained for about two years. He has devoted much of his time to the study of chemistry and chemical problems, both in industry and otherwise. Since graduating from Technology he has been employed as a research chemist and

has taken a course at Harvard in investment work (R. 345, 400, 490).

Malcolm M. Bowen was elected a trustee of Aldred Investment Trust on November 18, 1941, at a shareholders' meeting and served continuously until enjoined. He prepared at Exeter Academy and then attended the Wharton School of Business at the University of Pennsylvania. He took courses in business administration, economics and finance, accounting, investments, insurance and industry. He then entered the investment business with Baker, Young & Company and worked for them about eight years doing analytical work, trading and salesmanship. He then was employed by the Boston Mutual Life Insurance Company as statistician and investment officer and continued there for almost ten years. For the past four years he has been home office representative of the John Hancock Mutual Life Insurance Company and his duties consist in part of the supervision of investment policies (R. 417-419, 201, 212-213).

Ezra D. Hart, who is a petitioner as trustee of Aldred Investment Trust but not individually, was elected a trustee of Aldred Investment Trust by the trustees on January 17, 1944. Mr. Hart graduated from Exeter Academy, then attended Harvard College, graduating therefrom in 1919. After graduating from Harvard he was employed in the construction business at Springfield, Massachusetts, and then was employed as a salesman by the Atlas Portland Cement Company for a period of about eight years. After leaving Atlas Portland Cement Company around 1930 he became associated with Old Colony Trust Company of Boston in its new business department and was so employed for a little over a year. Following that he went into the securities field with Tifft Brothers as a salesman for a period of about two years. He then became associated with Gordon B. Hanlon & Company as a salesman of securities in 1933 and continued with this company until December,

1942. His work required a great deal of travelling, and because of the gasoline shortage he left this employment and became engaged in production control in defense work for the Simplex Wire and Cable Company. This work consisted of planning, scheduling and controlling the manufacture of submarine cable for harbor defense equipment. He is forty-eight years old (R. 540, 541).

John L. Arnold was elected treasurer of Aldred Investment Trust at a meeting of the trustees on November 25, 1941, and continued to serve in this capacity up to and including the time of the commencement of this action. He never became a trustee. Mr. Arnold was graduated from Bowdoin College in 1934 with a degree of Bachelor of Arts, and then attended Harvard Business School, graduating therefrom in 1937 with the degree of Master of Business Administration. While at Harvard Business School he majored in investment management and finance. He then attended Northeastern School of Law, graduating *cum laude* with a degree of Bachelor of Laws, passed the Massachusetts Bar Examination, and became a member of the Massachusetts Bar. Upon graduation from Harvard Business School he was employed by Estabrook & Company in the statistical department, doing statistical and investment research work, being employed by that firm for a period of about four years. He was then employed as treasurer of Aldred Investment Trust and later of Eastern Racing Association (R. 392, 393, 394).



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# In the Supreme Court of the United States

OCTOBER TERM, 1945

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No. 645

ALDRED INVESTMENT TRUST AND GORDON B. HANLON, ROBERT P. LORING, ELTON N. HANLON, W. EDWARD HIGBEE, JOHN L. ARNOLD AND MALCOLM M. BOWEN, INDIVIDUALLY AND AS TRUSTEES AND OFFICERS OF ALDRED INVESTMENT TRUST, AND EZRA D. HART, AS TRUSTEE OF ALDRED INVESTMENT TRUST, PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

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*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT*

---

**BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION  
IN OPPOSITION**

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OPINIONS BELOW

The opinion of the Circuit Court of Appeals (R. 1101-1114), affirming the judgment of the United States District Court for the District of

Massachusetts, is reported in 151 F. 2d 254. The opinion of the District Court (R. 100-119) is reported in 58 F. Supp. 724.

#### JURISDICTION

The judgment of the Circuit Court of Appeals for the First Circuit was entered on September 17, 1945 (R. 1114). The petition for a writ of certiorari was filed on December 7, 1945. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. § 347 (a)).

#### STATUTE INVOLVED

Section 36 of the Investment Company Act of 1940 (54 Stat. 841, 15 U. S. C. § 80a-35) provides:

#### INJUNCTIONS AGAINST GROSS ABUSE

SEC. 36. The Commission is authorized to bring an action in the proper district court of the United States or United States court of any Territory or other place subject to the jurisdiction of the United States, alleging that a person serving or acting in one or more of the following capacities has been guilty, after the enactment of this title and within five years of the commencement of the action, of gross misconduct or gross abuse of trust in respect of any registered investment company for which such person so serves or acts:

(1) as officer, director, member of an advisory board, investment adviser, or depositor; or

(2) as principal underwriter, if such registered company is an open-end company, unit investment trust, or face-amount certificate company.

If the Commission's allegations of such gross misconduct or gross abuse of trust are established, the court shall enjoin such person from acting in such capacity or capacities either permanently or for such period of time as it in its discretion shall deem appropriate.

#### QUESTIONS PRESENTED

1. Does the evidence support the district court's finding, affirmed by the circuit court of appeals, that the officers and trustees of the petitioner investment trust have been guilty of "gross abuse of trust" within the meaning of Section 36 of the Investment Company Act?

2. Where all except one of the officers and trustees of an investment trust, including the controlling stockholder thereof, were permanently enjoined from serving as such officers and trustees upon a finding that they had been guilty of a "gross abuse of trust" within the meaning of Section 36 of the Act, did the circuit court of appeals err in upholding the district court's power to appoint receivers for the trust?

#### STATEMENT

The petitioners seek review by this Court of the judgment of the United States Circuit Court of Appeals for the First Circuit which affirmed a

judgment of the United States District Court for the District of Massachusetts granting in full the relief sought by the plaintiff Securities and Exchange Commission. The district court permanently enjoined each of the individual petitioners, except Hart,<sup>1</sup> from serving or acting in the capacity of trustee or officer of the petitioner Aldred Investment Trust, and also appointed receivers for the Trust with the power either to reorganize the capital structure of the Trust or liquidate the Trust and distribute the assets to such creditors, debenture holders, and shareholders of the Trust as may be entitled thereto (R. 96, 119).

The Securities and Exchange Commission brought this action pursuant to Sections 36 and 42 (e) of the Investment Company Act of 1940 (54 Stat. 789, 841-2, 15 U. S. C. §§ 80a-35 and 80a-41 (e)) ("the Act"), administration of which was entrusted to the Commission by Congress. Jurisdiction of this action was conferred upon the district court by Section 44 of the Act (15 U. S. C. § 80a-43). The circuit court of appeals found that the evidence supported the finding of the district court that the individual defendants who

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<sup>1</sup> The court did not enjoin Ezra D. Hart, who joins in the petition as trustee of the Trust, because the court found that the evidence was insufficient to warrant a finding of "gross abuse of trust" by him since he did not become a trustee of Aldred until after certain misconduct on the part of the other trustees had already occurred (R. 119). Except as specifically noted, reference to the "petitioners" will mean the petitioners other than Hart.

were enjoined had, as trustees and officers of Aldred Investment Trust, been guilty of "gross abuse of trust," within the meaning of Section 36 of the Act.

A suit, referred to as the *Stratton* case (R. 1102), had earlier been instituted by certain security holders of the Trust charging the management with gross abuse and misconduct and seeking the appointment of a receiver. The record upon which the present judgment was entered consists of evidence taken both in that suit and on the Commission's application. Since the relief granted on the Commission's application was identical with that requested by the security holders, the complaint of the security holders in the *Stratton* case was dismissed without prejudice (R. 119).

Aldred Investment Trust (sometimes referred to herein as "Aldred" or the "Trust") is registered with the Securities and Exchange Commission pursuant to Section 8 of the Act (15 U. S. C. § 80a-8), and is classified under the definitions contained in Sections 4 and 5 of the Act as a closed-end, non-diversified management investment company (R. 3, 21, 100). The Trust was established by an Agreement and Declaration of Trust in 1927 as a common law trust under the laws of Massachusetts (R. 3, 21, 35, 101). The trust indenture vested in the five organizing trustees and their successors legal title to the trust

estate, absolute control, complete management and investment discretion (R. 35-66, 101). In case of vacancies the remaining trustees are authorized to appoint a successor trustee but a majority of the trustees or the holders of 25% of the common voting shares may at any time call a shareholders' meeting at which holders of a majority of the shares may supersede or re-elect the trustees in office or fill any vacancy (R. 37, 101). The trust may be terminated at any time by a written instrument signed by all the trustees although the shareholders are not empowered to end the Trust until 75 years from the date of the trust agreement or until 21 years after the expiration of numerous specified lives in being (R. 62-3, 101).

Debentures of the Trust now outstanding and held by the public amount to \$5,900,000, mature in 1967, and bear interest at  $4\frac{1}{2}\%$ . To each debenture is attached one no-par value common share in the Trust for each \$100 principal amount of the debenture so that 59,000 non-detachable common shares are outstanding. The Trust also issued 112,500 free common shares not attached to any debentures (R. 3, 21, 101). These were issued to Aldred and Company, investment bankers and sponsors of the Trust (R. 4, 22, 101). All common shares, whether non-detachable or free, have equal voting rights, share for share (R. 50, 102).

The purpose and declared investment policy of the Trust, until January, 1944, when the Hanlon management effected certain changes, was to invest its assets in readily marketable securities issued by public utility and industrial corporations, and the trust portfolio was made up largely of such securities (R. 102, 1004, 684-7, 628-9, 625-7, 622-3, 619-20, 616-7, 613-4, 609-10, 606-7, 867-8, 870, 872-3).

The Trust Agreement provides that no investment by the Trust shall be deemed improper because of its speculative character, or the commitment therein of an unusually large proportion of the Trust estate, or because the trustees or officers of the Trust may have an interest in, or stand to profit from, the investment (R. 44-5, 101). However, pursuant to the requirement contained in Section 17 (h) of the Act,<sup>2</sup> the Trust Agreement was amended on October 8, 1941 (R. 975, 980-1) to provide, *inter alia* (R. 66):

Nothing in this Agreement and Declaration of Trust as heretofore amended shall protect any trustee or officer of the Trust against any liability to the Trust or to the

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<sup>2</sup> Section 17 (h) required the elimination from the Agreement and Declaration of Trust of "any provision which protects or purports to protect any director or officer of such company against any liability to the company or to its security holders to which he would otherwise be subject by reason of willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of his office."

shareholders of the Trust to which he would otherwise be subject by reason of wilful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of his office after October 31, 1941.

At all times since 1937 the Trust has been insolvent in that the asset value of the Trust has been substantially less than the principal amount of debentures outstanding (R. 103, 949, 891-904, 136-7, 286-7, 330, 397). In consequence the common stock has of course had no asset value since 1937. From 1940 through 1943 the Trust could not meet its interest requirements out of income. The deficiency of income for those years amounted to \$479,775 out of the total interest requirements of \$1,062,945. In order to prevent default on the interest payments on outstanding debentures and possible foreclosure and termination of the trust by debenture holders, capital assets were sold to make up the differences (R. 874, 876, 889-91, 893, 897, 246-262, 331-2, 193-4, 209-10).

On October, 1941, Gordon B. Hanlon (referred to herein as "Hanlon"), a securities broker and one of the petitioners, purchased a controlling block of 110,000 common unattached shares (64.11% of all common shares) of the Trust. This purchase was made at a public auction conducted on behalf of a foreclosing pledgee of shares issued originally to Aldred and Company. Hanlon paid \$10,000 plus about \$9,000 in transfer

taxes for the shares (R. 5, 24, 215-7). At the time of Hanlon's purchase the Trust's assets had a market value of only \$2,110,000 as against \$5,900,000 face amount of debentures outstanding (R. 887-8).

The conduct of Hanlon after he acquired control of the Trust and the conduct of the management he installed is discussed in the opinions of the district and circuit courts (R. 104-18, 1105-1114). The courts' findings are discussed in detail in the argument.

The court below sustained the district court's finding and the Commission's contention that Hanlon and the others enjoined with him had been guilty of gross abuse of trust. In general, the district court found that Hanlon's conduct and management of the Trust had been "calculated to further his own personal advantage" and that transactions had been made which were "motivated by self-interest" rather than the interests of the debenture holders of the Trust for which Hanlon was a fiduciary. As to the others enjoined, the court found that they aided Hanlon, participated in his activities and shared the benefits (R. 100-119).

The circuit court of appeals reaffirmed all of the district court's "detailed findings with respect to the management of the Trust" by the petitioners, which had been made "after careful

consideration of the evidence" (R. 1105) and stated, *inter alia*:

The appellants [petitioners] challenge none of the facts upon which the decision below rested. Their objections extend only to the inferences drawn from the admitted facts to which they join the assertion that the District Court omitted consideration of certain other relevant facts which it should have taken into account. We have examined the record carefully, and in our opinion the only inferences permissible from the evidence and testimony presented at the trial are clearly to the effect that Hanlon and his associates during the period they had the management of the Trust were motivated primarily by ideas of personal gain. From the moment they took over they embarked upon a course of action which culminated in the acquisition of Eastern Racing Association. That transaction enabled Hanlon and his associates to elect themselves directors and officers of the Suffolk Downs horse-racing track, a business about which they knew nothing but which carried the certain prospect of handsome salaries (R. 1106).

\* \* \* \* \*

The findings of the District Court, amply supported by the evidence, reveal a course of conduct that was motivated by self-interest and personal advantage and the calculated denial of fiduciary obligations. At no time during the period the appellants

managed the trust did the shares they relied on for control represent any equity position. The trust assets belong to the debenture holders. In effect the appellants have been using their control of other people's money to enrich themselves through the perquisites of such control. In our opinion the court below properly found them guilty of "gross abuse of trust" within the meaning of § 36 of the Act. (R. 1112.)

#### ARGUMENT

The petition presents "two principal questions" (see Pet. p. 5).<sup>3</sup> The first question and the one upon which major emphasis is placed raises merely the issue whether, as the petition states, "the evidence warrants a finding" (see Pet. p. 5) that the individual petitioners have been guilty of gross abuse of trust. The issue is purely one of fact as to which two lower courts have stated that the evidence "amply supported" the finding of gross abuse of trust (R. 1112) and indeed the circuit court of appeals stated that the finding of gross abuse of trust represented "the only inferences permissible" (R. 1106). No conflict between circuits exists and there is no rea-

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<sup>3</sup> One other question mentioned in the petition (see Pet. p. 6, par. (9)) is not briefed and was not mentioned in the court below. In addition, it is without merit on its face. Notice to shareholders is not necessary in a suit to remove directors for misconduct and, certainly, if it were, petitioners have no standing to complain on their behalf.

son for further review by this Court of the sufficiency of the evidence, particularly where a strong showing has been made that the evidence is overwhelming in favor of the conclusion of the lower courts. *Anderson v. Abbott*, 321 U. S. 349, 356.

The other question raised by the petitioners relates to the right of the district court to appoint receivers. While the question is of importance to the administration of the Investment Company Act, the decision of the lower courts is clearly correct. There is no conflict of decisions and further review by this Court is not necessary. We therefore urge that the petition for certiorari be denied.

1. The circuit and district courts properly held that the evidence fully established that Hanlon and the other enjoined petitioners grossly abused their trust. We submit that the courts below were not compelled to believe the protestations of Hanlon and the other petitioners that they acted always with a view to the best interests of the debenture holders when the evidence overwhelmingly indicated the contrary. The circuit court of appeals specifically found on this issue that "Their protestations of good faith are not borne out in the record of what they did" (R. 1107).

Briefly summarized, the findings and evidence as to Hanlon's conduct and that of the other peti-

tioners whom he controlled with respect to the management of the Trust, are as follows:

Hanlon purchased the controlling block of the stock of Aldred Investment Trust at a time when this stock was valueless, asset-wise, and would continue to be so unless and until the value of the Trust assets increased to nearly treble its value at the time of the purchase (R. 887, 888). Furthermore, the earnings of the Trust were and had been insufficient to meet the annual interest requirements on the outstanding debentures (R. 331-2). Hanlon knew these facts at the time (R. 214, 337, 338). But he also knew that these securities carried voting control of the insolvent Trust "with the attendant power," as the courts below noted, "to elect and remove trustees and officers, to fix the compensation of the latter, and to dominate completely the policies of the Trust." Hanlon's only apparent motive for the purchase was to enjoy personal emoluments of control of the \$2,100,000 of trust assets. His subsequent actions confirm that this was in fact his motive.

Hanlon immediately ousted the existing board of trustees and elected as a new board of trustees and as officers of the Trust himself and certain employees, relatives and friends (R. 1105) none of whom had theretofore had any responsibility for the management of other people's funds. At all times the trustees were subject to Hanlon's

wishes and directions. Hanlon and his friends received salaries as trustees and as officers of the company. Hanlon himself was made president of the company at a salary of \$5500 and later \$6900 per year (R. 999, 714, 347). The office of the Trust was moved to Hanlon's brokerage office in Boston and the Trust was charged rentals of \$410 per month, which were paid to Hanlon.<sup>4</sup> Through his salary and receipt of \$4,920 per year for office space (R. 999, 714), Hanlon was able during the first two years he controlled Aldred to draw out more than the \$20,000 he had paid for his controlling interest in the Trust.

With the Trust facing the threat of bankruptcy proceedings and unable to pay interest on the outstanding debentures except by sale of portfolio securities, Hanlon sought to effectuate a plan of reorganization which would relieve him of the pressure of the interest requirements of the debentures. He and his nominees in the management prepared several plans which would have left his control undisturbed but would have had the effect of making the payment of debenture interest contingent upon earnings (R. 907-13, 915, 937, 940, 997, 450-3, 569, 578-81, 150-1, 236-7, 649, 650-1, 918-36, 658, 943, 970, 662). However, when Hanlon submitted his plans to the Securities

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<sup>4</sup> Hanlon charged the Trust \$410 per month for the use of the office space and facilities of Hanlon's brokerage firm, plus the use of one additional adjoining room for which Hanlon paid \$40 monthly rent (R. 128-9, 132-3).

and Exchange Commission, the Commission took the position that any plan would be grossly unfair which did not leave the debenture holders in full control of the Trust (R. 938, 658). The Commission stated to Hanlon at the time that if he attempted to carry out his proposed plans the Commission would be forced to institute injunction proceedings pursuant to the authority vested in the Commission by Section 25 (c) of the Act to enjoin the consummation of any plan found to be "grossly unfair" (R. 911-4, 653-4, 659, 660, 664).

None of these plans was ever actually submitted to the debenture holders by Hanlon. Although Hanlon had advised the Commission that liquidation was the only feasible alternative to recapitalization (R. 908, 910, 923), no recapitalization was effected and no plan for liquidation was ever proposed. As the court below said (R. 1108):

The District Court recited these negotiations [with the S. E. C.] as evidenciary of the conflict of interest between the appellants' concern with the perquisites of control and a proper concern for the interest of the debenture holders which dictated either reorganization or liquidation. As the court pointedly remarked: "Hanlon, since he had no equity standing in the enterprise, could not gain by liquidating, and stood to lose the more than

\$10,000 per annum he was receiving from the Trust."

Unable to relieve himself of the interest requirements, the Hanlon management continued during 1942 and 1943 to sell high grade portfolio securities to pay debenture interest and management expenses (R. 1108; Pet. p. 14)<sup>5</sup> when serious consideration of the interests of the debenture holders would have indicated the necessity of a fair recapitalization or liquidation.

Hanlon also sought the purchase of *controlling* interests of speculative businesses. This course involved (1) the possibility of strengthening his investment position in the Trust if the speculation turned out favorably, and (2) prospects of salaries for himself and nominees in the businesses passing under the control of the Trust. He tried to purchase for the Trust control of a horse or dog track from which he could also obtain high salaries for himself and his nominees (R. 288-9).

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<sup>5</sup> Referring to the district court's findings with approval, the court below said (R. 1108):

"The court considered this to be a return of capital in the guise of interest. It pointed out that no technical act of default could occur so long as the appellants could sell securities and pay out the proceeds as 'ostensible interest;' that this left the debenture holders 'helpless under the terms of the debenture instrument to halt the dissipation of their assets,' and concluded that so long as the 'personal advantage' of the appellants stood in the way 'the debenture holders could not expect relief either by way of bona fide recapitalization or liquidation.'"

Hanlon and his management finally obtained an option to purchase control of Eastern Racing Association ("ERA") which operates the Suffolk Downs horse-racing track in Boston. The price paid for the controlling block of ERA stock, a total of \$1,195,184, was \$80 a share (R. 31, 9, 360-1), substantially in excess of the market price for small blocks of that stock which were then being bought and sold at between \$50 and \$60 a share (R. 507). The difference in price represented a premium paid for securing control, as Hanlon frankly admitted (R. 302, 1109).

Special premiums are sometimes paid for "control" blocks—a primary reason for this being that such control carries with it the power to designate officers and directors and fix compensation. But the debenture holders of the Trust had and have nothing to gain by the premium paid for this control—the Trust itself could not acquire offices, salaries or the like by virtue of the control. Only the individual petitioners in their private capacity could expect to benefit by such control.

Upon completion of the purchase, members of the Hanlon management promptly elected themselves directors of ERA and Hanlon was elected president (R. 762-9). The evidence is clear that Hanlon and some of his associates contemplated receiving salaries from Eastern Racing Association, some of which would be between \$25,000 and

\$50,000 per year (R. 759-61, 1040-1, 1042-3; 369).

To obtain the large sum of \$1,195,184 to purchase the illiquid and highly speculative Eastern Racing stock, the Hanlon management sold large blocks of the best and most marketable securities of the company (R. 31, 9, 247-8, 250-1, 252, 253, 333, 1005, 1109). Two of these securities sold were the same securities which Hanlon had previously stated to the S. E. C. should not be disposed of hastily and in large blocks (R. 947-8, 662). Some of the shares were sold in a negotiated transaction at two points below the market (R. 278, 279).

The effects of this purchase of ERA stock were several. It involved the sale of liquid assets in order to buy frozen assets, stock which did not have a good and ready market, thus tying up the funds of the insolvent trust in a non-marketable security (R. 801, 276-9, 357).<sup>6</sup> The extremely speculative character of the race track stock, due largely to the industry's uncertainties because of changing public opinion and governmental regulation (R. 304, 113, 801-3),

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<sup>6</sup> Compare the rule that a trustee must give primary consideration to the marketability of a proposed investment in the light of the probable date of termination of the Trust. See *Restatement of the Law of Trusts*, Vol. I, § 227 m, page 651. The termination of the Aldred Trust through bankruptcy was an admittedly imminent possibility. See the proposed letter to debenture holders (Pl. ex. 25, R. 662, 944).

lends further emphasis to the disregard of the interest of the public security holders. It was their money not his that was risked. Cf. *Tower Hill-Connellsville Coke Co. of West Va. v. Piedmont Coal Co.*, 64 F. 2d 817, 821-822 (C. C. A. 4), certiorari denied, 290 U. S. 675.

The investment in a race track, the acquisition of control of such an enterprise, the shift of 30% of the assets of the Trust from readily marketable and conservative securities to such an illiquid and speculative block of securities at a time when the Trust was insolvent was an extraordinary step involving both a radical departure from previous investment policy and a conflict of interest between Hanlon and the beneficiaries. Thus even the most open course of dealings would not justify the action taken. In any event it called for the frankest disclosure. But, as the district court stated, "Instead of fulfilling this obligation to the holders of the debentures, the defendants pursued a positive program of concealment." (R. 117.)

The investment of approximately a third of the assets of the Trust in a single company, outside the public utility industry, and the assumption of controlling functions in that company was at variance with the declared purposes of the Trust and it was necessary to obtain stockholder approval of the change. The change was voted at a shareholders' meeting upon wholly inadequate notice. The only indication was a statement in

the notice of the meeting that one of the purposes of the meeting would be "to consider and vote upon future investment policy for the Trust." (R. 591.) As the district court stated, this was "a masterful bit of understatement" (R. 117).

The district court found also that inquiries from shareholders and members of the public were avoided and evaded in order that no objection to the program of acquisition and management of the race track should be made until the racing season was over (R. 316-7, 1043-4, 778, 1046-7, 111). The elaborate precautions taken to see that investors did not discover what was happening do not bespeak a management honestly concerned for the debenture holders and attempting to do its best in the interest of those holders.

The record leaves no doubt that the petitioners enjoined had participated in all the major activities which constituted the gross abuse of trust. They voted Hanlon the salaries, the rental for office space; they approved the policy of selling assets to pay interest and expenses in order to avoid liquidation; they were fully aware of Hanlon's negotiations for the stock of Eastern Racing Association and approved the purchase of that stock; they accepted office in Eastern Racing Association. To all of Hanlon's plans they gave hearty assent and their votes were unanimous on all matters needed to effect those plans. As the court below stated: "We are not disposed to ques-

tion the conclusion of the District Court that 'at all times the trustees have been subject to Hanlon's wishes and directions'. It is apparent from the record that Hanlon's was the guiding hand and that the other appellants readily fell in with all his plans for the management of the Trust" (R. 1106). Although petitioners argue that there was no evidence to support this finding (see Pet. p. 21), it is in fact conceded that all the trustees were selected by Hanlon; that by his ownership of the controlling stock of the corporation Hanlon could oust the trustees and place into office other trustees of his choice merely by calling a new stockholders' meeting on thirty days' notice (R. 160, 206-7), a procedure he had followed in ousting the trustees who were in office before he acquired the stock of the trust. The trustees he selected owned neither stock nor debentures of the Trust and had no interest in the Trust other than their positions and the salaries paid to them (R. 125, 188, 202, 320-4). On all of the matters as to which abuse of trust was found there is no indication of any dissent on the part of any of these trustees and all votes were unanimous (see, e. g., R. 160-1, 190). The trustees-petitioners were all relatives, employees or close personal friends of Hanlon (R. 122-4, 189, 201-3).

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Some mention should be made of the standard of conduct imposed on fiduciaries by the Investment Company Act. Section 36 of the Act em-

powers a district court of the United States to enjoin an officer or director of a registered investment company from acting in such capacity or capacities upon a finding that said person has been guilty of "gross misconduct or gross abuse of trust." As was properly held below, the interpretation of "gross misconduct or gross abuse of trust" as used in this section depends not only upon relevant common law principles of fiduciary duties but also upon the declarations of policy as set forth by Congress in Section 1 (b) of the Act.

In substance and as applied to this case, the standard laid down is, as the courts below held, that officers, directors and controlling stockholders of investment companies and trusts are fiduciaries and that in exercising their fiduciary capacities they are required to act in accordance with the standards generally applicable to fiduciaries. Primarily, they must manage the Trust in the interest of the beneficiaries of the Trust and not in their own personal interest. However, the Investment Company Act, while reaffirming the fiduciary standards to which managers of investment trusts are held, does not purport by Section 36 to disqualify officers and directors from further service in cases of mere technical violations of their trust, such as the making in good faith of an investment which is prohibited by the provisions of the trust or similar minor deviations from the high standards of a fiduciary. Rather, Sec-

tion 36 deals only with a "gross abuse" of trust and is intended to cover such substantial deviation from the obligations of trusteeship as would indicate that the officers and directors involved cannot be entrusted with the management of other people's money without substantial danger that the trust will be turned to the benefit of the manager rather than to the benefit of all classes of security holders. The statutory declarations of purposes in the Act (Section 1 (b)) is, as the circuit court of appeals stated (R. 1111), a codification of the fiduciary obligations imposed upon directors and officers of investment trusts. Thus, for example, Section 1 (b) (2) of the Act provides that the Act is to be construed to eliminate the evils which exist "when investment companies are \* \* \* managed, or their portfolio securities are selected, in the interest of directors, officers, \* \* \* or other affiliated persons thereof, \* \* \* rather than in the interest of all classes of such companies' security holders."<sup>7</sup>

<sup>7</sup> Other portions of Section 1 (b) provide that \* \* \*

"It is hereby declared that the policy and purposes of this title, in accordance with which the provisions of this title shall be interpreted, are to mitigate and, so far as is feasible, to eliminate the conditions enumerated in this section which adversely affect the national public interest and the interest of investors."

and that the national public interest and the interest of investors are adversely affected

"(1) when investors \* \* \* receive dividends upon, vote, refrain from voting, sell, or surrender securities issued

This standard as well as the substantially identical common law standard is to be considered in determining whether there has been such substantial deviation from that standard as to constitute a gross abuse of trust.

Petitioners in effect state (see, e. g., Pet. 17) that it is perfectly proper under the indenture in this case for the trustees and officers to enter into transactions on behalf of the Trust which have as their purpose the serving of their individual interests as opposed to the interests of the debenture holders. This contention, as the courts below found, is untenable. Nothing in the in-

by investment companies without adequate, accurate, and explicit information, fairly presented, concerning the character of such securities and the circumstances, policies, and financial responsibility of such companies and their management;

\* \* \* \*

(3) when investment companies \* \* \* fail to protect the preference and privileges of the holders of their outstanding securities;

\* \* \* \*

(5) when investment companies, in keeping their accounts, in maintaining reserves, and in computing their earnings and the asset value of their outstanding securities, employ unsound or misleading methods, or are not subjected to adequate independent scrutiny;

(6) when investment companies are reorganized, become inactive, or change the character of their business \* \* \* without the consent of their security holders;

\* \* \* \*

(8) when investment companies operate without adequate assets or reserves."

denture permits such action and both ordinary standards applicable to fiduciaries and the Investment Company Act prohibit such action. See *Pepper v. Litton*, 308 U. S. 295, 311. In the leading case of *Carrier v. Carrier*, 226 N. Y. 114, 125-126, Judge Cardozo said of a trustee acting under an instrument which granted absolute and uncontrolled discretion in the matter of investment: "His discretion, however broad, did not relieve him from obedience to the great principles of equity which are the life of every trust." Had there been any doubt that fiduciary obligations could not be destroyed by language of a Trust instrument, the reiteration of those obligations by the Congress in the Investment Company Act would have resolved that doubt. *Philadelphia, Baltimore & Washington R. R. Co. v. Schubert*, 224 U. S. 603; *Continental Insurance Co. v. United States*, 259 U. S. 156.

As the evidence amply supported the findings of the courts below that Hanlon's activities and those of his associates were motivated primarily by the prospects of personal financial advantage, contrary to the interests of the debenture holders, the courts below properly found that the petitioners (except Hart) had been guilty of "gross abuse of trust" and properly held that petitioners should be enjoined under Section 36 of the Act.

2. Petitioners contend that the circuit court of appeals erred in affirming the district court's ap-

pointment of receivers even if the petitioners, except one, were properly enjoined from acting as officers and trustees of Aldred (Pet. 21-30).

The courts below found that Hanlon and most of his associates had grossly abused their trust and enjoined them from continuing as officers or trustees of the Trust. In substance, the judgment was that Hanlon and his associates could not be trusted with the management of other peoples' money. However, such an injunction alone would be thoroughly ineffective so long as Hanlon retained the controlling stock of the Trust. For an injunction which permitted Hanlon to nominate another group of trustees subject to his domination and control would merely perpetuate the situation which resulted in the abuse and might be expected to result in a repetition of the suit. The only complete and adequate remedy against the repetition of the abuses which the district court found to exist was a basic reorganization or liquidation of the Trust, so that Hanlon would no longer have control of assets which belong exclusively to the debenture holders. This could be done either by a reorganization which would wipe out the stock and place control of a new trust or corporation in the hands of existing debenture holders or by some program of liquidation which would place the assets or other proceeds in the hands of the debenture holders to whom they belong free from the influence of Hanlon. And this

is just what the district court below did. It appointed receivers for the Trust "with the power either to reorganize the capital structure of the Trust or liquidate the Trust and distribute the assets to such creditors, debenture holders, and shareholders of the Trust as may be entitled thereto" (R. 119). Petitioners' argument that no receivership is necessary is, strangely enough, based on the fact that Hanlon still owns the majority of stock and can place a new management in office (Pet. 21). To this is added the argument that Hart is not enjoined (*id.*). But the district court refused to enjoin Hart only because he did not become a trustee until after the Eastern Racing Association transaction was almost complete (R. 119). It was not because he was free of Hanlon's domination. Hart's continued availability does not in any way remove Hanlon's control of the voting securities or lessen the likelihood of abuse by him through Hart and other nominees not yet enjoined. Compare *Bernstein v. New Jersey Bankers' Securities Co.*, 156 Atl. 768, in which the New Jersey Court of Errors and Appeals affirmed a decree for the appointment of a receiver on the ground that the voting control of the corporation was in the hands of an individual who had caused the company to be mismanaged by such officers and directors as he had selected.

Petitioners, however, place their major emphasis not on the contention that a receivership is not a proper remedy for the evils found to exist, for it is indeed obvious that it is not only proper but necessary. Rather they pitch their argument on the more technical ground that even though a receivership is proper, the Commission has no standing to ask for such relief (Pet. 22 *et seq.*). But Section 36 of the Act, in giving the Commission jurisdiction to seek injunctions because of gross abuse of trust, authorizes resort to equity. And once this jurisdiction of equity has been invoked it is familiar doctrine that the court will retain the case until full justice is done and that to this end it may use all the powers inherent in a court of equity. On this point the court below rightly stated (R. 1112-3):

Hanlon's voting control represents no equity interest in the Trust, and to permit him to remain in control would be to perpetuate the very conditions that brought about this suit. In granting relief the District Court relied upon its equity power to appoint receivers with power either to reorganize or liquidate the Trust. In the light of the circumstances surrounding this case the only effective means of protecting the interests of the debenture holders was to remove Hanlon from the control of the trust assets which do not belong to him. § 36 invokes the equity power of the Federal Court and that calls into play its

inherent powers where necessary to do justice and grant full relief. The appointment of receivers in the case at bar was an appropriate exercise of the court's inherent equity power. *Graham v. Railroad Company*, 102 U. S. 148, 161; *Kitchum v. MacDonald*, 85 F. (2d) 436 (C. C. A. 3d, 1936) cert. den. 299 U. S. 595; *Tower Hill-Connellsville Coke Co. v. Piedmont Coal Co.*, 64 F. (2d) 817, 823 (C. C. A. 4th, 1933); *S. E. C. v. Fiscal Fund*, 48 F. Supp. 712 (1943). *S. E. C. v. Long Island Lighting Co.*, 148 F. (2d) 252 (C. C. A. 2d, 1945) relied on by the appellants, turned on a question of jurisdiction of the subject matter which question is not present in the instant case.

The petitioners place much emphasis on the opinion of the Second Circuit Court of Appeals in *S. E. C. v. Long Island Lighting Co.*, 148 F. 2d 252 (Feb. 23, 1945), quoting at length from the opinions of Judges Simons and Hutcheson, who constituted the majority in that case (Pet. 24-28). That case is, however, not in point. It presented the question of the jurisdiction of a federal court to give injunctive relief at the suit of the Securities and Exchange Commission pursuant to the Public Utility Holding Company Act where the relief sought was to preserve the status quo pending an administrative hearing. Whether or not the respondent was subject to regulation under the Act was contingent upon a future administra-

tive decision to revoke an exemption previously granted by the Commission. The majority opinion of Judge Simons first found inapplicable, in view of the then exempt status of respondent, the statutory provisions authorizing a Commission suit to enjoin a "violation" of the Act and then urged the absence of any authority for a federal court "to protect by injunction a jurisdiction not presently existing, merely because upon speculative and problematical circumstances, such jurisdiction may at some uncertain time in the future, arise." Nevertheless, that opinion concludes that the problem there resolved was "not free from doubt." That decision has no application to the present situation where there is no question of the jurisdiction of the court over the subject matter, where there is no question of the right of the Securities and Exchange Commission to institute suit against gross abuse of trust, and where the only question is the extent of the relief which a court of equity should grant against a proven abuse.<sup>5</sup>

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<sup>5</sup> This is not, however, to concede the authority of the *Long Island Lighting Co.* case, for we believe the dissenting opinion of Judge Clark in that case to be more cogent than the opinion of the majority judges. In support of this position we petitioned this Court for certiorari and certiorari was granted, 324 U. S. 837, March 26, 1945. After the Commission had filed its brief here, and before argument, the Long Island Lighting Company accepted a ruling of the Commission revoking its exemption, registered as a holding company, and took all steps necessary to render the case moot. Accordingly, on April 30 this Court entered the following

It is, therefore, submitted that a receivership was essential to do justice in the present case; that adequate authority exists for the appointment of receivers in such cases; and that the court had adequate power to appoint such a receiver on the application of the Securities and Exchange Commission.

#### CONCLUSION

For the foregoing reasons it is respectfully submitted that the petition for a writ of certiorari be denied.

J. HOWARD McGRATH,  
*Solicitor General.*

ROGER S. FOSTER,  
*Solicitor,*

MILTON V. FREEMAN,  
*Assistant Solicitor,*

ARNOLD R. GINSBURG,  
*Attorney,*  
*Securities and Exchange Commission.*

JANUARY, 1946.

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order, *per curiam*: "It appearing that the cause has become moot, the judgment of the Circuit Court of Appeals is vacated and the case is remanded to the District Court with directions to dismiss the complaint."